

**AGENCY FOR INTERNATIONAL DEVELOPMENT  
PPC/CDIE/DI REPORT PROCESSING FORM**

ENTER INFORMATION ONLY IF NOT INCLUDED ON COVER OR TITLE PAGE OF DOCUMENT

**1. Project/Subproject Number**

497-0357

**2. Contract/Grant Number**

497-C-00-98-00045-00

**3. Publication Date**

November 2002

**4. Document Title/Translated Title**

Reforming Indonesia's Ports

**5. Author (s)**

1. David Ray
2. Richard Blankfeld
- 3.

**6. Contributing Organization (s)**

Nathan/Checchi Joint Venture/PEG Project

**7. Pagination**

22

**8. Report Number**

PEG 100

**9. Sponsoring A.I.D. Office**

ECG, USAID/Jakarta

**10. Abstract (optional - 250 word limit)**

As the world's largest archipelago nation, Indonesia requires a well-developed and efficiently run ports sector. Producer competitiveness in both national and international markets, internal distribution efficiency and national economic cohesiveness and integrity are influenced by port sector performance. Development of adequate port facilities is especially important in the outer regions in Indonesia where the lack of transport facilities may diminish the incentive to produce an agricultural surplus. Despite its critical importance to the national economy, Indonesia does not have a port system that performs well from the perspective of its users. This paper identifies a number of factors undermining port performance, giving particular attention to problems associated with the lack private sector participation as well as the overall lack of competition in the ports system. These problems are in large part due to the continuing dominance by state-owned enterprises in the provision of port services and the current legal and regulatory environment that constrains competition both within and among ports. With the continuing growth in trade through Indonesia's ports and the increasing rate of containerization, there is an urgent need to modernize the port system. There is a broad range of initiatives and measures needed to achieve this objective: two of which are considered in this paper. The *first* is an accelerated program of privatization, designed and implemented to ensure the competition-driven efficiency benefits of increased private sector participation. The *second* is the deregulation of Indonesia's many private ports such that they can compete with the main public ports.

**11. Subject Keywords (optional)**

- |                   |                  |
|-------------------|------------------|
| 1. Indonesia      | 4. Privatization |
| 2. Maritime Ports | 5.               |
| 3. Deregulation   | 6.               |

**12. Supplementary Notes**

**13. Submitting Official**

C. Stuart Callison, Chief of Party

**14. Telephone Number**

011-62-21-520-1047

**15. Today's Date**

January 23, 2003

.....DO NOT write below this line.....

**16. DOCID**

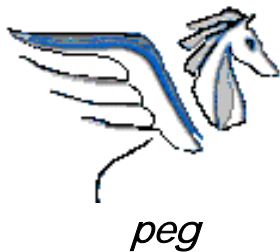
**17. Document Disposition**

DOCRD ☐ INV ☐ DUPLICATE ☐

Technical Report

# Reforming Indonesia's Ports

By David Ray and Richard Blankfeld



**Prepared for:**

Ministry of Industry and Trade and  
Ministry of Communications and Transportation

**Submitted to:**

USAID/ECG, Jakarta, Indonesia

**Submitted by:**

Nathan/Checchi Joint Venture  
Partnership for Economic Growth (PEG) Project  
Under USAID Contract #497-C-00-98-00045-00  
(Project #497-0357)

**November 2002**

## TABLE OF CONTENTS

<b>REFORMING INDONESIA'S PORTS.....</b>	<b>3</b>
INTRODUCTION .....	3
<i>Background of Study</i> .....	3
<i>Structure and Management of the Port System in Indonesia</i> .....	4
<i>Port Traffic</i> .....	5
KEY PROBLEMS IN THE PORT SECTOR.....	8
<i>Poor Performance</i> .....	8
<i>Physical Constraints</i> .....	9
<i>Lack of a Transshipment Port</i> .....	9
INCREASING PRIVATE SECTOR PARTICIPATION IN INDONESIAN PORTS .....	12
<i>Completed Port Concessions</i> .....	13
<i>Constraints on PSP</i> .....	15
<i>Strategies for Increasing PSP</i> .....	16
INCREASING COMPETITION THROUGH DEREGULATION .....	17
<i>Deregulation of special ports</i> .....	18
<i>Decentralization of the Ports Sector</i> .....	19
<i>The Case of Cilegon</i> .....	20
<i>Port of Cigading (Krakatau Steel)</i> .....	20
CONCLUSION.....	21

### The authors:

David Ray, Ph.D.  
Domestic Trade Advisor  
Partnership for Economic Growth (PEG)  
Ministry of Industry and Trade  
USAID – Nathan Associates  
Email: [dray@pegasus.or.id](mailto:dray@pegasus.or.id)

and

Richard Blankfeld  
Vice-President and Transport Specialist  
Nathan Associates, Washington  
Email: [Rblankfeld@nathaninc.com](mailto:Rblankfeld@nathaninc.com)



# Reforming Indonesia's Ports

David Ray and Richard Blankfeld  
Partnership for Economic Growth<sup>1</sup>, Jakarta  
USAID – Nathan Associates

## **Introduction**

As the world's largest archipelago nation, Indonesia requires a well-developed and efficiently run ports sector. Producer competitiveness in both national and international markets, internal distribution efficiency and, more generally, national economic cohesiveness and integrity are, to a significant extent, influenced by port sector performance. Development of adequate port facilities is especially important in the outer regions in Indonesia where the lack of transport facilities may diminish the incentive to produce an agricultural surplus.

Despite its obvious critical importance to the national economy, Indonesia does not have a port system that performs well from the perspective of its users. This paper identifies a number of factors undermining port performance, giving particular attention to problems associated with the lack private sector participation as well as the overall lack of competition in the ports system. These problems are in large part due to the continuing dominance by the state in the provision of port services (through the activities of state owned enterprises), and the current legal and regulatory environment that effectively constrains competition both within and among ports.

With the continuing growth in trade through Indonesia's ports, and the increasing rate of containerisation of that trade, there is an urgent need to modernise the port system. There is a broad range of initiatives and measures that need to be taken by the government to achieve this modernisation objective: two of which are considered in this paper. The *first* is an accelerated program of privatisation, designed and implemented in such a way as to ensure the competition-driven efficiency benefits of increased private sector participation. The *second* is the deregulation of Indonesia's many private ports such that they can compete with the main public ports.

## **Background of Study**

This paper pulls together and draws upon the work on port sector reform by long and short-term consultants working on the USAID-GOI project, the *Partnership for Economic Growth* (PEG), over the 2001-02 period. The initial focus of this work was to consider how improvements in the maritime sector could better facilitate flows of international and domestic trade. At an early stage

---

<sup>1</sup> PEG is a USAID-funded Project. The views expressed in this report are those of the authors and not necessarily those of USAID, the U.S. Government or the Government of Indonesia.

in this work, it became clear that most serious constraints confronting the maritime sector were sourced to problems in the ports.

The shipping sector, unlike the ports sector, is very competitive and responsive to demand, due mainly to deregulation efforts in the late 1980s. However, no matter how well run and competitive a shipping line may be, it will not be profitable if its ships must spend a considerable proportion of their working time queuing outside, or berthed at congested ports.

This is the reality confronting many shippers, particularly those involved in inter-island trade, as the sail time between destinations is relatively short<sup>2</sup>. For example it takes around two days to sail from Jakarta to Pontianak<sup>3</sup>. Average turn-around time in the port of Pontianak is a little under two days, whilst in Jakarta approximately three and half days<sup>4</sup>. This suggests that a ship on this particular route would be spending at least half, maybe three-quarters of its time in port. This example can be multiplied many times over.

A simple average of turn-around time for all ports handling inter-island cargo in Indonesia is approximately 4-5 days. Thus congestion and other associated inefficiencies that result in delays at port is a serious problem confronting shippers as it leads to widespread underutilization, and therefore a lack of profitability, of their vessels. It is for this reason we focus on port issues.

## **Structure and Management of the Port System in Indonesia**

In all, Indonesia has around 2000 ports. This includes 500 ‘non-commercial’ ports that tend to be unprofitable and only half of which can accommodate vessels. In addition, there are approximately 100 ports, including 25 major ports, which are deemed as ‘commercial ports’ and are controlled by the four state owned Indonesian Port Corporations (IPC) I, II, III and IV. There are also 1400 ‘special purpose’ or private ports that are also regulated by the PELINDO companies. These special ports serve private sector needs such as industry, mining, fishing etc.

From 1960 to 1963, the National Port Company was responsible for the management of all public ports. In 1963, the National Port Company retained responsibility of commercial aspects of the public ports, while the Port Authority carried out port operational activities. From 1969 through 1983, the Port Management Board, according to Government regulations 1/1969 and 18/1969, carried out management of the port system.

In 1983, public commercial port management was separated into four Public Port Corporations according to the following geographic criteria.

---

<sup>2</sup> Most Indonesian shippers are involved in domestic trade. Local shippers carry 50-55% of Indonesia’s domestic cargo, but only 3-4% of the country’s international cargo. However these figures are exaggerated by the fact due to the imposition of tariffs and VAT on imported vessels, as well as efforts in the past to protect the government owned shipyard PT PAL, many shippers tend to lease foreign flag vessels

<sup>3</sup> According to the latest schedules provided for the various shipping lines in the June 10, 2002 edition of the ‘Indonesia Shipping Gazette’.

<sup>4</sup> These figures are based upon the turn-around time for inter-island vessels in 1999 (Pontianak 46.5 hours and Tanjung Priok, Jakarta 82.3 hours) made available by the Ports and Dredging section of the Ministry of Transport.

- **IPC 1** is headquartered in Medan and has responsibility for the commercial ports of the three provinces of Aceh, North Sumatra and Riau. The corporation has 22 ports. The Riau port of Batam, just to the south of Singapore, is not included among the corporation ports. In 1991, the public port corporations were changed from a public corporation to state-owned company.
- **IPC II** is headquartered at Tanjung Priok, the port of Jakarta. The corporation has responsibility for commercial seaports of eight provinces, namely, West Java, West Kalimantan, West Sumatra, Bengkulu, Jambi, South Sumatra, Lampung, and Bangka-Belitung. IPC II has recently assumed control of the ports in Batam.
- **IPC III** is headquartered at Surabaya's port of Tanjung Perak. The corporation has ports in eight provinces, namely, East Java, Central Java, Bali, West Nusa Tenggara, East Nusa Tenggara, Central Kalimantan and Southern Kalimantan. The corporation has 19 ports with branch offices and 21 subsidiary ports.
- **IPC IV** is headquartered at the Ujung Pandang port of Makassar. The corporation has a total of 21 ports serving a huge area stretching from East Kalimantan to Irian Jaya, and including Sulawesi and the Maluku islands.

The above geographic criteria also determine the area of control for each of the IPC's regulatory authority over the activities of the private 'special purpose' ports.

In 2002, the government is considering plans to merge and consolidate the four IPCs into one or two port management corporations. Reasons cited for the proposed merger include the more efficient use of management resources, lower administration costs, and the potential to leverage the financial resources of the profitable IPC II and IPC III for development of port facilities in the former IPC I and IPC IV<sup>5</sup>.

## Port Traffic

According to the Ministry of Transport, approximately 90% of Indonesia's external trade is transported via sea, and roughly half of that trade is through the main port in Jakarta, Tanjung Priok. International and domestic traffic handled at IPC ports in 1999 is presented in Table 1 on the previous page. The 95 IPC ports handled 342.0 million tons of cargo, with 65 percent of the traffic handled at IPC II (34 percent) and IPC III (31 percent). Together IPC II and III account for 84 percent of all imports and 50 percent of all export traffic IPC ports.

More than 43 percent (148.6 million tons) of total international and domestic cargo handled at the IPC ports in 1999 was liquid bulk. Another 28 percent (95.2 million tons) of the traffic was handled as dry bulk. The remaining 29 percent of cargo (98.7 million tons) was handled as break-bulk general cargo, bagged cargo unitized cargo or containerized cargo.

---

<sup>5</sup> Various commentators have also suggested that the main reason behind the proposed merger is to strengthen the balance sheet of the largest port corporation IPC II, weakened by the large debt necessary to finance the delayed project to develop Bojonegoro in West Java as the country's primary trans-shipment port – see for example comments by the Secretary General of the Indonesian National Ship-owners Association (INSA) in '*Merger pelabuhan hasilkan benturan visi*' *Bisnis Indonesia*, Wednesday 23<sup>rd</sup> January 2002, page 5.

**Table 1. Int'l and Domestic Container Traffic 1999 (000 tons)**

Item	Pelindo				Total
	I	II	III	IV	
<u>Imports</u>					
General cargo	266.7	1,659.4	1,435.8	42.2	3,404.1
Bag cargo	1,252.2	2,715.0	2,064.7	149.7	6,181.6
Unitized cargo	266.4	1,697.5	213.6	13.6	2,191.1
Dry bulk	1,088.5	6,880.9	3,946.4	365.3	12,281.1
Liquid Bulk	2,424.4	5,632.0	7,268.8	2,001.9	17,327.1
Container cargo	496.9	5,439.9	818.6	-	6,755.4
Subtotal	5,298.2	24,024.7	15,747.9	2,572.7	47,643.5
<u>Exports</u>					
General cargo	789.2	3,708.0	2,488.3	86.2	7,071.7
Bag cargo	200.4	2,373.1	676.6	479.7	3,729.8
Unitized cargo	2,171.7	2,553.1	283.6	825.5	5,833.9
Dry bulk	7,484.7	7,212.0	21,780.2	5,034.2	41,511.1
Liquid Bulk	23,788.4	2,822.3	1,084.9	10,838.9	38,534.5
Container cargo	988.4	6,279.6	1,299.7	-	8,567.7
Subtotal	35,422.8	24,948.1	27,613.3	17,264.5	105,248.7
<u>Domestic -Unloading</u>					
General cargo	1,805.6	5,938.0	6,665.6	1,293.6	15,702.8
Bag cargo	1,247.5	2,602.7	1,441.6	2,131.3	7,423.1
Unitized cargo	362.9	941.6	250.5	337.5	1,892.5
Dry bulk	2,389.4	11,705.8	11,433.3	1,356.2	26,884.7
Liquid Bulk	4,983.9	13,424.5	20,274.5	6,765.1	45,448.0
Container cargo	343.4	1,353.0	1,823.6	2,323.9	5,843.9
Subtotal	11,132.7	35,965.6	41,889.1	14,207.6	103,195.0
<u>Domestic -Loading</u>					
General cargo	688.8	3,928.2	4,279.1	485.8	9,381.9
Bag cargo	514.2	2,246.8	1,968.6	721.4	5,451.0
Unitized cargo	1,293.6	594.9	722.5	91.0	2,702.0
Dry bulk	1,366.1	8,875.2	3,545.2	712.7	14,499.2
Liquid Bulk	18,873.5	12,897.6	9,034.2	6,529.1	47,334.4
Container cargo	205.3	2,477.8	2,755.5	1,085.9	6,524.5
Subtotal	22,941.5	31,020.5	22,305.1	9,625.9	85,893.0
<u>Total all cargo</u>					
General cargo	3,550.3	15,233.6	14,868.8	1,907.8	35,560.5
Bag cargo	3,214.3	9,937.6	6,151.5	3,482.1	22,785.5
Unitized cargo	4,094.6	5,787.1	1,470.2	1,267.6	12,619.5
Dry bulk	12,328.7	34,673.9	40,705.1	7,468.4	95,176.1
Liquid Bulk	50,070.2	34,776.4	37,662.4	26,135.0	148,644.0
Container cargo	2,034.0	15,550.3	6,697.4	3,409.8	27,691.5
Total	74,795.2	115,958.9	107,555.4	43,670.7	341,980.2

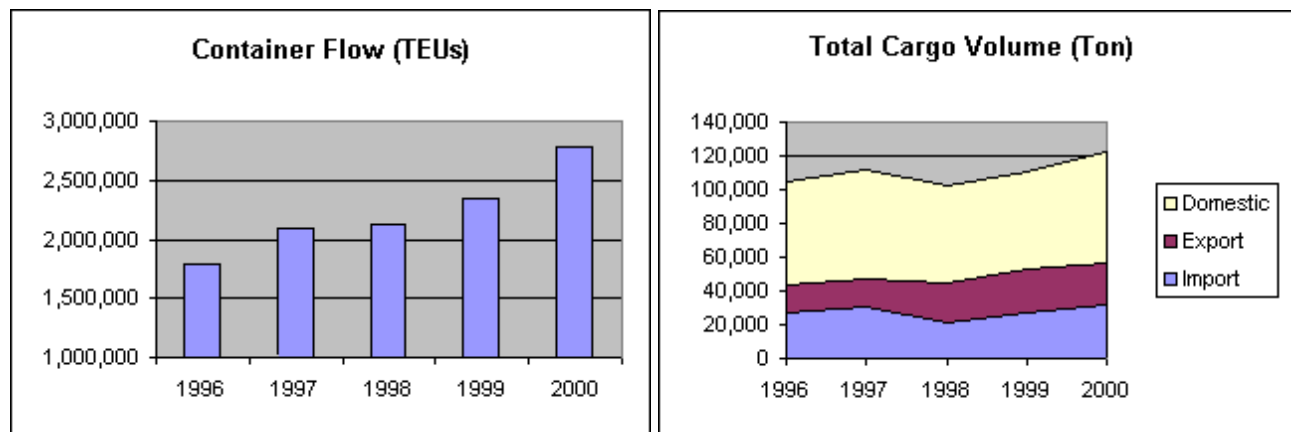
Source: Direktorat Pelabuhan Dan Pengerukan, Sub Direktorat Pengembangan Pelabuhan, Rekapitulasi Operasional Pelabuhan, PT (Persero) Pelabuhan Indonesia, Tahun 1999, Jakarta 2000.

Industry sources indicate that containerized cargo has been increasing rapidly in recent years for both the international and domestic trade with growth rates in excess of 15 percent. Graph 1. below shows the growth in total cargo volume and container traffic through IPC II ports over the 1996-2000 period. Ideally the data should describe cargo volume in containers (as opposed to just their number). Nevertheless average annual growth rates over the 5 year period of 4.3 percent for total cargo traffic and 11.7 percent for containers (TEUs) suggests increasing rates of containerisation.

Despite this move toward containers, the share of Indonesian international and domestic cargo containerised remains low by international standards. For the IPC ports, roughly 28 percent of the non-bulk cargo handled in 1999 was in containers (35 percent for international cargo and 22 percent for domestic cargo).

While a detailed commodity and trade route analysis has not been performed, it would seem reasonable given industry standards and current trends in Indonesian trade that the share of non-bulk cargo shipped in containers could double within the next 10 years. Coupled with the normal growth of overall international and domestic trade, the volume of container cargo to be handled at Indonesian ports it may well triple in the next 10 years. The accommodation of this anticipated rapid growth in container traffic presents both opportunities and challenges for the Indonesian port sector.

**Graph 1. Total Cargo and Container Traffic through IPC II Ports, 1996-2000**





## **Key Problems in the Port Sector**

### **Poor Performance**

The performance of Indonesian ports in delivering services to users such as shippers and freight-forwarders, is relatively poor. This is reflected in a number of key indicators such as berth occupancy rate, vessel turn-around time and working time ratio.

Overall, the simple average for berth occupancy rate for all ports in 1999 (the latest data available) was 59 percent, well beyond the maximum internationally acceptable standard of 40 percent<sup>6</sup>. This suggests that with increased growth in trade volumes by sea, and the increasing containerisation of that trade, dramatic increases in delay and waiting times can be expected in the near future. Waiting times will likely increase most dramatically at the smaller ports with only a few berths.

Average turn-around time, as discussed earlier, also suggests port performance, with ocean-going vessels requiring on average 76 hours (or slightly over 3 days) in port, and 120 hours (or 5 days) on average for inter-island ships.

Working time as a percentage of turnaround time averages a very low 26 percent for oceangoing vessels and 37 percent for inter-island vessels. This means that for the time a vessel is in port it is only being serviced (i.e. unloaded/loaded) for around a half to a third of that time. This non-working time is explained in large part by the manner in which labor is used at ports which effectively institutionalizes underutilization of port facilities and limits the potential for efficiency improvements. In many ports, only one-shift of labor is provided and opportunities for overtime are limited<sup>7</sup>. For those ports that are meant to operate on a 24-hour basis, six hours out every 24 are being lost because of rigid break periods not staggered to ensure continual servicing of vessels.

In addition to these key causes of port inefficiency, another problem is delay due to unfairness and corruption in berth assignment. Many shippers interviewed complain of having to deal with too many institutions, groups and individuals in getting their consignments through the ports. In the case of the container terminal in Jakarta, shippers expect one-stop services to cut out the need to deal, and therefore transact, with a variety of parties, which raises costs and leads to delays<sup>8</sup>.

---

<sup>6</sup> Berth occupancy rate is the percentage of time vessels are berthed at port.

<sup>7</sup> A recent report in the media by the Ship-owners Association (INSA) claims that due to a shortage of working time, approximately 6-10% of export shipments are not loaded in time, and must be loaded on the next ship available during the following work period, thus raising handling costs. See '*Pengapalan barang ekspor di Priok terganggu*', *Bisnis Indonesia* 23 August 2002, page 1.

<sup>8</sup> The Director General for Customs, Permana Agung Drajjattun, noted in a recent seminar that export and import activities in the main port of Jakarta involves no less than 30 institutions (including port authorities, labour groups, shipping associations, transport officials, security officials etc) See '*Ekspor-impor di pelabuhan melibatkan 30 institusi*' *Bisnis Indonesia*, 9 November 2001.

## Physical Constraints

Another major problem constraining port performance is the lack of infrastructure available in each port. Only 16 of the 95 commercial ports have container terminals, equipped with the necessary cranes and other moving equipment. In many on the smaller commercial ports ships must use own gear. In other cases particular shipping lines keep own their equipment at the port, but to ensure their own competitive advantage do not make it available to other shippers<sup>9</sup>.

Space for container storage and stuffing is extremely limited in many Indonesian ports. As a result, users typically must transport their containers to and from their factories or yards raising overall distribution costs.

Only a few ports have separate facilities for cargo and passenger ships resulting in the frequent displacement of the former by the latter. Only after the passenger vessel departs, can the cargo ship re-berth and resume operations. In ports with high berth occupancy rates, the simultaneous presence of passenger and cargo vessels results in even further delays, and increases the total turn-around time for cargo vessels.

Balikpapan, for example, is a very congested port handling over 50,000 TEUs in 2002 with just two berths, and a total port area of less than 3 hectares. Like many other ports in Indonesia, the port of Balikpapan is poorly located where road access is via the busy city centre. Such congestion problems are exacerbated by the arrival of passenger vessels 48 times a month. When this occurs, any cargo vessel currently loading or unloading must leave the berth for at least 5 hours<sup>10</sup>.

Port depth appears to be a major problem in virtually every port in Indonesia. Indonesia's particular geographic and climatic conditions results in very few natural deep-water harbours and a river system prone to serious siltation that restricts port depth<sup>11</sup> For many ports, continuous dredging is a very real and expensive reality. Where dredging is not feasible, vessels often have to wait until high tide until entering the port, which leads to more downtime of vessels.

## Lack of a Transshipment Port

Currently, most Indonesian exports and imports moving by sea are shipped via the port of Singapore. Large transoceanic ships do not make direct calls at Indonesian ports and most international shipping services from Indonesia are merely feeder services to Singapore. Even most of Indonesia's intra-Asia trade must be transshipped through Singapore. Development of an

---

<sup>9</sup> It is interesting to note that these shippers must still pay various fees to the local IPC for the use of their own equipment.

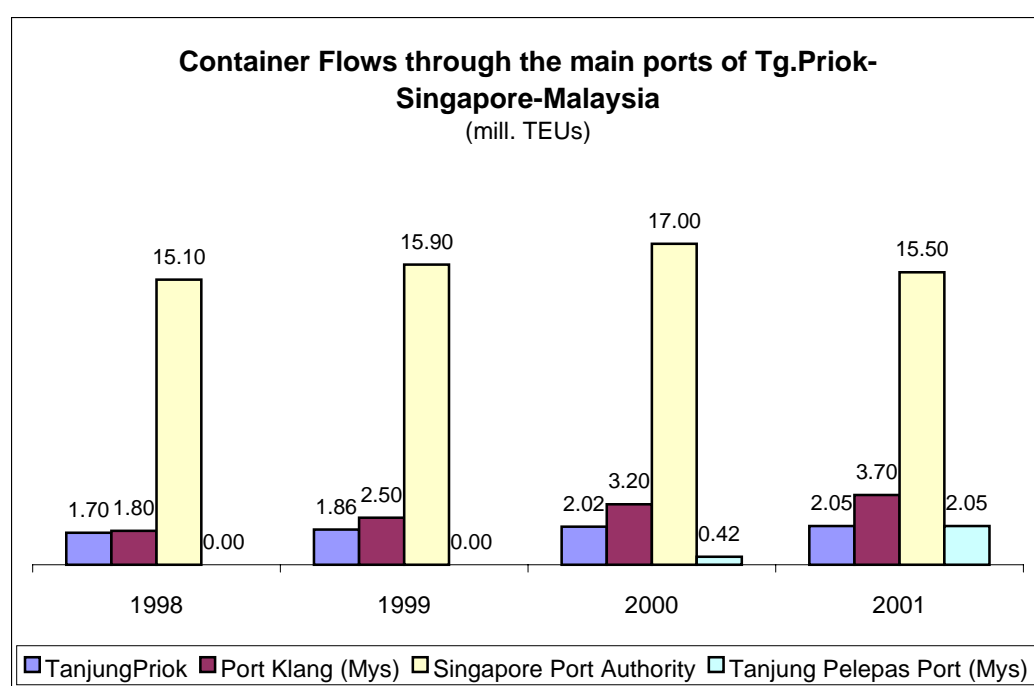
<sup>10</sup> Such congestion problems impact adversely upon the hinterland economy. Cement distributors in Balikpapan for example complain that bottlenecks within the port mean that certain cement products might be unavailable for weeks at a time. The problem is that to unload a vessel carrying cement takes up to 10 days, and to ensure that other vessels (including passenger vessels) get access to the port, only one ship can unload cement at any one time.

<sup>11</sup> See for example "Siltup disrupts port operation in Indonesia" Indonesia Shipping Gazette, May 6 2002, page 11; and "Lima pelabuhan alami pendangkalan" Bisnis Indonesia, 12 April 2002 Page 14, both of which described the substantial dredging activities required in 2002 to keep IPC II ports operational.

effective transshipment port understandably represents an important priority for the government's maritime policy. As shown in graph 2, container flows in the region continue to be dominated by Singapore. However, Singapore's share has recently been dented by the emergence of Tanjung Pelepas in Malaysia

JICA (1999) notes that the volume of containers accommodated at the port of Tanjung Priok (i.e., around 1.5 to 2 million TEUs per annum) is at the threshold level for attracting transoceanic service direct calls. The JICA study concludes that provided only that Tanjung Priok and the nearby port development area of Bojonegara are developed to provide sufficient capacity and high performance standards, the Tanjung Priok-Bojonegara port complex can become

**Graph 2 Container flows through regional ports**



**Table 2 Share of Regional Container Traffic**

Port	1998	1999	2000	2001
Tanjung Priok	9%	9%	9%	9%
Port Klang (Mys)	10%	12%	14%	6%
Singapore Port Authority	81%	78%	75%	67%
Tanjung Pelepas Port (Mys)	0%	0%	2%	9%

Source: Jakarta Container Terminal

Indonesia's international hub container port, and much of the feeder service to Singapore will no longer be necessary<sup>12</sup>. Indonesia would be able to follow Malaysia's lead in taking market share away from Singapore (table 2)

The same JICA Study estimates that development of Tanjung Priok Bojonegara, together with Tanjung Perak in Surabaya as a secondary hub, has the potential for reducing Indonesia's feeder shipping costs by 39 percent and transpacific shipping costs by 14 percent, in comparison with continued full reliance on Singapore for making transoceanic shipping service connections.

The proposed location of the first trans-shipment port in West Java is obvious given that the Western part of Java represents the country's greatest concentration of industrial activity. However as the Eastern regions continue to develop, there should be growing demand for shipping services in Sulawesi, Papua as well as West and Eastern Nusa Tenggara. Eventually, Indonesia will need a second transshipment port that can service these eastern provinces of Indonesia. Whilst it is important that in the medium term the TPB complex accommodate sufficient container traffic to attract direct calls by transoceanic liner shipping services, in the long term a port in the eastern part of Indonesia could be usefully developed to also attract similar sized liner ships. JICA (1999) notes that the Port of Tanjung Perak (the country's second largest port) is too close to Tanjung Priok to serve as an effective second transshipment port, and instead identifies the port of Bitung in North Sulawesi as a possible candidate.

Progress in developing Bojonegara port has been slow. At the height of the financial crisis in 1997, the government of Indonesia suspended all work on the Bojonegara port, leaving IPC II, having purchased the necessary land, with a large debt<sup>13</sup>. This regulation has since been lifted. Recent work on the port has been limited to some feasibility studies being done by donors and some minor planning work with local governments

There is also concern from the government about the capacity of the proposed port to deliver the competition-driven improvements in services, as the first stage of the port has been committed to the same business entity, HPH, which now controls the two terminals in Tanjung Priok<sup>14</sup>. This suggests that another opportunity to promote competition in the ports system has been lost (see next section regarding the privatisation of the terminals at the port in Jakarta). HPH has little

---

<sup>12</sup> Note that a portion of Indonesia, namely northeastern Sumatra and West Kalimantan, because of proximity to Singapore, will likely continue to use Singapore as a hub container port.

<sup>13</sup> This was unfortunate for IPCII, as it had already taken on a large debt in the form of medium term notes to secure the necessary 460 hectares of land at Bojonegoro. The notes have recently matured (April 2002), however the IPC is unable to repay the \$US 123 million owing. There have been numerous reports in the media that IPC II has been able to cover this debt by accepting a loan from the Tanjung Priok concessionaire Hutchison-Whampoa Ltd in exchange for a ten-year extension of that concession. This has been denied by the company as well as the IPCII, which it maintains, is proposing a debt restructuring deal to the government – see for example reports in *Business Indonesia* March 6 2002, April 4, 8, 10 and 16. Despite the SOE's difficult financial position, it is interesting to note that IPC II continues to fulfill what is known as its public service obligations. In 2001 for example, IPCII extended to small businesses and cooperatives Rp 6 billion in soft loans as well as Rp 770 million in training - see *Business News* 13 March 2002.

<sup>14</sup> According to government sources interviewed, this agreement was made before the JICT concession was finalized.

incentive to move ahead to develop Bojonegara at this time. It holds the development rights for the important first stages of the Bojonegara port and has a monopoly on the two container terminals in Tanjung Priok, which are being further developed and integrated. Until capacity is reached in Jakarta, there is no need to sink new investment in developing the port.

Further complicating efforts to develop a viable trans-shipment port in Indonesia, is the proposal by the Ministry of Transport for the development of a number of minor trans-shipment ports such as Kupang, in East Nusa Tenggara, Batam near the island of Singapore, Bitung (mentioned above), Biak in Papua and Sabang off the north coast of Aceh. In each case it is difficult to see any of these ports in the immediate future having sufficient volume, let alone facilities, to attract and accommodate large transoceanic ships. Notwithstanding the medium-term long run possibility for Bitung mentioned above and the special case of Sabang discussed below, the development of each port is unlikely to extend beyond that of providing feeder services.

#### **BOX 1**

##### **SABANG AS A TRANS-SHIPMENT HUB**

Sabang, given its strategic location at the mouth of the Malacca Straits, has long been touted as a likely trans-shipment hub. Interest in Sabang has been renewed with the announcement by the Thai government of a feasibility study for the Kra Canal to be located on the narrow part of the country's southern peninsula. Such a canal would provide a direct link between the Indian Ocean (Andaman Sea) and the Gulf of China South China Sea. This would shorten sea journeys by approximately 1000 km or 5 days sailing time, as there would be no need to enter the Malacca straits. According to the *Indonesia Shipping Gazette* (May 27 2002, p 11) this could lead to savings of anywhere from US \$ 37,000 to US\$ 120,000 per voyage (It is interesting to note that Nathan Associates performed an economic and feasibility analysis of the Kra canal in 1973. The study concluded that the canal was not feasible.)

However a number of factors constrain the development of either a feeder or hub port in Sabang in the short-medium term. *First*, there is no hinterland economy for the port to service. Sabang is an island connected to the mainland part of Aceh via irregular and infrequent ferry services (each journey requires at least two hours sailing time). Moreover, Aceh is not a major production centre and is highly dependant upon goods imported from other provinces. Traders interviewed in Banda Aceh prefer to import via land transport from Medan, North Sumatra and would regard shipping through the proposed port in Sabang as a costly alternative.

*Second*, the development of Sabang as either a hub or feeder port would require significant investment. Given present fiscal pressures, adequate funding from the government would be unlikely. The only real option is through private investment, and this is also unlikely to be dissuaded by the continuing uncertain security environment in Aceh. *Third*, even if the Sabang is developed as a hub port, it is not clear that shippers, particularly those in Java, will opt to send their cargo all the way up to the north coast of the island of Sumatra, when more efficient, and possibly lower cost trans-shipment options are available in Singapore and Malaysia (Tanjung Pelepas), or even the Tanjung-Priok Bojonegara complex, if developed,

### ***Increasing Private Sector Participation in Indonesian Ports***

Earlier it was noted that with expected container traffic likely to at least double, if not triple, over the next decade, there is an urgent need to modernise the port system. As the government is no longer willing to provide budgetary funds for the development of IPC ports, the only real option is to expand the role of the private sector in the ports system. Increasing private sector participation is necessary not only as a means to fund this modernisation program, but also as a means to introduce worlds best practice, technology and know-how. Moreover, if designed and

implemented carefully, increasing private sector participation should result in the injection of much needed competition into the port sector, leading to better port services at lower prices.

Indonesian law prohibits the outright sale of ports to the private sector, but allows for the privatisation of operations and activities within ports, such as container terminals. In this regard a number of options are available ranging from management contracts (with little or no private sector investment) to leasing of existing infrastructure, joint operation, joint venture and BOT arrangements. The present investment regulations allow 95 percent foreign ownership of port facilities, although there have been recent attempts to reduce this to 49 percent.

A general rule of thumb within the privatisation literature is that whenever privatisation is carried out in a competitive environment (or in a situation where abuses of market power are effectively constrained by the regulatory environment) there are net welfare benefits to the community by way of better quality services (or goods), delivered in a more responsive and at lower prices. Privatisation in a non-competitive environment typically results in the transfer of a monopoly from the public sector to the private sector, with little or no benefits for the consumer or user, although such privatisations tend to be priced at a premium, and therefore generate larger proceeds for government. Indonesia's port privatisations to-date in Surabaya and Jakarta (discussed below) more generally fall into this latter category, although the Surabaya concession is widely acknowledged within the industry as providing the best port services in the country.

### **Completed Port Concessions**

Indonesia's first experiences with port privatization were initiated during and influenced by the economic crisis of 1997-1998. A key objective of these privatizations was to raise funds by the sale of attractive public enterprises in order to fill a \$1.5 billion gap in the government budget. Other objectives of the privatization program such as to improve efficiencies, introduce new technologies and management, provide capital for expansion and to foster competition were of secondary importance.

In this section the principal features, characteristics and results of the transactions completed for concessions of the container terminals at the Tanjung Priok in Jakarta and the Tanjung Perak in Surabaya are considered.

#### *Tanjung Priok Container Terminal JICT-Koja (Jakarta)*

As noted earlier, Indonesian law prohibits the outright sale of Indonesia public ports. However, it was determined that the award of long-term concession for a specific facility within a port was acceptable under Indonesian law. Thus for the privatization of terminals I and II of the main container facility in Tanjung Priok port, a new subsidiary Jakarta International Container Terminal (JICT) was established under IPC II in 1998. JICT was awarded a concession to manage and operate the Jakarta Container Terminal for a period of 20 years. Potential strategic investors for 51 percent ownership of JICT were solicited through a competitive bidding process. Bidders were to have at least 5 years experience in container terminals with a combined throughput of at least 400,000 TEUs; assets of at least US\$ 100 million; tangible net worth of at least

\$100 million, and no ownership of a competing container port of 200,000 TEUs within 1,500 km of JICT.

The successful bidder Grosbeak (a subsidiary of Hutchison Port Holdings or HPH) paid US\$ 215 million in cash plus non-cash contribution of operating software and technical support valued at US\$ 28 million. HPH reported that in April 1999 the port was handling 18-19 moves per crane per hour. With new equipment and training provided by HPH, by late 2000 the port was consistently handling 24-25 moves per crane per hour, which represents an acceptable international standard for gantry crane productivity. Equipment availability is near 90 percent.

Following the purchase of the 51 percent stake of JICT in April 1999, HPH subsequently secured a 48 percent stake in the adjacent Koja Terminal in September 2000. In April 2002, there were various reports in the media that the term of the container terminal concession was increased from 20 years to 30 years in conjunction with a \$100 million loan from Hutchison Whampoa Ltd to IPC II. However, as noted earlier, JICT management has denied these reports.

The port of Tanjung Priok (Jakarta) is relatively more efficient than most other Indonesian ports, and vessels often require just a single day at this port. Both international and domestic shipping operators express regret, however, that the government missed an opportunity to establish a competitive situation in the port by entering into contracts with two container terminal operators that are both subsidiaries of the same foreign company. The general view from users, is that privatization resulted in the transference of a monopoly from public to private hands with no major improvement in port services. There are regular reports in the media of alleged abuse of market position<sup>15</sup>. There are also concerns that the planned merger of the four IPCs will result in further monopolistic behavior and is otherwise inconsistent with the broader plans to decentralise the ports sector<sup>16</sup>.

#### *Tanjung Perak Container Terminal TPS (Surabaya)*

Within IPC III, container terminal operations were organized into a separate unit called UTPK (*Unit Terminal Peti Kemas* – Container Terminal Units) in April 1992. UTPK has three sub-units, TPK I which handles inter-island containers, TPK II which handles ocean-going containers and TPK III which is programmed to handle ocean-going containers once TPK II reaches capacity.

Similar to the experience in Tanjung Priok, a new subsidiary company PT Terminal Petikemas Surabaya (PT. TPS) was established in April 1998 as a limited liability company by IPC-III to facilitate privatization of UTPK. All existing equipment and employees of UTPK were transferred to PT. TPS, while TPS paid lease payments for fixed assets. In May 1998, IPC-III commenced the privatization program for TPS. Invitations were sent to 38 international bidders

---

<sup>15</sup> There were a series of reports in the *Bisnis Indonesia* daily in April documenting claims by various parties that the recently combined JICT-Koja terminal was threatening shipping lines that send their ships to the conventional terminals at the Tanjung Priok port will be denied later access to their container terminal (see for example *Bisnis Indonesia* 19 April 2002).

<sup>16</sup> See for example, 'Merger PT Pelabuhan sebabkan tarif jadi mahal (Port company merger will cause high tariffs)' *Bisnis Indonesia* 19 March 2002; 'Merger pelabuhan hasilkan benturan visi' (Merger causes divergence in visions for port development) *Bisnis Indonesia*, 23 January 2002.

of whom 9 expressed their interest. In March 1999, four of the nine were classified as preferred bidders to proceed to the next rounds. A two-stage process was established consisting of non-cash aspects in round one (administrative, legal, and technical operational) and cash offer in round two. The winner was determined by the highest cash offer among the preferred bidders that passed round one.

Main non-cash criteria were 10 years experience in container terminals with a combined throughput of at least 600,000 TEUs; assets of at least US \$100 million; no ownership of major ports within 1,000 nautical miles of TPS. In April 1999 P& O Australia Ports Pty, Ltd was confirmed as the winning bidder with an offer of US\$ 173.76 million for 49 percent ownership of TPS.

In several regards, the concession for UTPK is considered a success. First, the transaction raised more funds than the \$136 million initially projected; second, P&O agreed to additional investments in the port to increase and upgrade the number of gantry cranes and other container handling equipment. This resulted in a boost in port efficiency and container-handling rates approached international standards. Further, by maintaining the private participation to 49 percent, P& O was able to avoid some of the political and labor issues that accompanied the transfer of JICT in Tanjung Priok.

However, the high value attained for the concession of UTPK also comes with some negative attributes. P&O has the right to develop a second terminal (*Kali Lamong*) at a nearby site if annual container volumes exceed 1.5 million tons. This precludes effective competition from other potential container terminal operators in the near- to mid-term. The high price and other annual payments required from P& O under the contract, place a premium on their generation of revenue and effectively constrains the passing along of any cost-savings in port operations to port users in terms of lower port tariffs or the prospect of smaller increases in port charges over time.

### **Constraints on PSP**

Despite the urgent need to modernise the port system, opportunities for further privatisations at this time are limited. The GOI's privatisation effort, which is otherwise obstructed by nationalist elements within the parliament and certain ministries, continues to focus on the banking sector, and has yet to fully consider opportunities in the industrial and infrastructure sector. The Ministry of Transport is, nevertheless, aware of the need to increase private sector participation and is prepared to move ahead to consider new concessions. However within the IPCs - which appear to be relatively influential on policy matters involving deregulation and privatization - there is both support and opposition to further concessions.

For example, there is broad consensus within the IPCs on the importance of private sector investment in the ports system. This is driven less by any underlying belief that the private sector is better placed than the public sector to provide port services, and more by the realization that any major modernization effort is unlikely to be government funded given present fiscal realities. Opposition to increased private sector participation in Indonesia's ports is grounded in concerns about the likely loss of control and influence (not to mention positions, employment and also



income – both formal and informal) as well as the added pressures of greater disclosure and transparency were operations privatized.

An added disincentive to support further port privatizations is that funds made available by private sector investors are unlikely to be transferred to either the IPCs or the Ministry of Communications for reinvestment back into the public port system. Rather, proceeds from privatization will most likely be used to ease pressure on the central government's budget, as was the case with the Tanjung Priok (Jakarta) and Tanjung Perak (Surabaya) concessions. To improve the overall incentive environment for port privatization, it may be advisable to allow the proceeds to be reinvested back into the ports system, particularly in areas in urgent need of modern port facilities and where there is uncertainty of adequate returns for private investors.

### **Strategies for Increasing PSP**

Two possible strategies to circumvent nationalist opposition within parliament and the entrenched interests of the IPCs are to pursue greenfield developments and to focus on the privatization of smaller ports. However each of these strategies bring with them their own set of problems.

Consider the case of greenfield development. There is an urgent need to relocate many primary and secondary ports, from highly silted rivers to deeper locations on the coast, and from congested urban and industrial areas to locations with appropriate transport connections and adequate room for storage.

There is clearly less political resistance to PSP in ports, when it is in the form of investment in new sites, as opposed to the sale of existing public assets. As a result there are currently many opportunities for private sector investors to develop greenfield sites. However serious constraints remain.

Perhaps the greatest constraint is being able to develop an appropriate landlord port model that effectively marries the interests of the private investor with that of the local and central governments and the particular IPC of the region. Most importantly an appropriate equity structure would need to be in place to ensure adequate returns to the private investor.

Under landlord port arrangements, the public sector retains ownership of the land and basic infrastructure and regulates port activities. The private sector has as its focus of the provision of services to vessels and cargo. However these institutional arrangements are unlikely to succeed if the public sector is unwilling to provide land, or basic infrastructure such as road connections, or perhaps to build breakwaters. This is a common problem in Indonesia. There are many local governments that would welcome new private sector developed container ports within their jurisdictions (and possibly to take equity positions in these ports), but few prepared to commit resources to freeing up land, or building necessary infrastructure.

One example is in Samarinda, East Kalimantan. The present port located on the river in the center of the city of Samarinda suffers from serious congestion problems (not to mention problems with the depth of the draft). A study funded by JICA has identified the location for a

new port facility, also on the river, but on the outskirts of Samarinda in an area called Palaran. However, all land required for the new facility is privately owned. The local government has estimated the land value at Rp 70 billion (or approximately US 7.8 million) but does not have the financial resources to purchase the land. An investor would be required to not only build the port but also purchase the land, and most probably to provide basic infrastructure. Not surprisingly there has been no substantial investor interest in the port.

A more likely model of a successful landlord arrangement can be found in the planned new port of Kariangau in Balikpapan, to the south of Samarinda, in the same province of East Kalimantan. Both the Provincial and district governments have set aside up 1500 hectares of land for the port and adjacent industrial estate. Moreover, the Provincial government is building a major road connecting the port-industrial estate area to the Balikpapan-Samarinda highway. Efforts are now being made attract private investors into a joint public-private partnership to develop Kariangau in Balikpapan as a gateway port for the province.

Another strategy for promoting private sector participation is to focus greater effort on facilitating private investment by local firms in smaller ports. There are, for example, important opportunities for investment by shipping operators in public port facilities, especially facilities for RORO vessels<sup>17</sup>. Current regulations, however, have constrained such investment.

As noted earlier, domestic shipping was deregulated in the late 1980s, and most firms in this sector are competitive and efficient. The sector's greatest concern remains the inefficiencies and bottlenecks in the public ports system. Unsurprisingly there are a number of shippers that are prepared to invest in developing their own port facilities (it was also noted that given the general lack of facilities, some shippers keep their own equipment stored and locked at various ports). However concerned to maintain equal access to facilities at public ports, the government currently bans investment in public ports by shipping operators.

Whilst ensuring non-discriminative treatment by port operators is important. Nevertheless a more effective mechanism may be available to achieve this objective, and at the same time open up investment opportunities. For example a new corporate entity could be formed to develop a port, whereby shipping companies wishing to use the terminal on a regular basis could then purchase shares in the newly formed company proportionate to their overall use of the port facilities. Appropriate regulatory instruments, such as the competition law (5/1999), could be used to prevent anti-competitive behavior.

### ***Increasing Competition Through Deregulation***

Increasing private sector investment is a necessary, but not sufficient condition for port sector modernisation in Indonesia. Considerable effort is also required in reforming the regulatory and institutional arrangements governing the sector. This would need to be done in such a way as to not only promote greater economic and legal certainty for investors, but also to help ensure that privatisation delivers the expected competition-driven efficiency benefits for consumers and

---

<sup>17</sup> RORO stands for roll-on roll-off. A RORO vessel carries both trucks and passengers. RORO shipping plays a critical role in facilitating domestic trade, and more generally in promoting economic integration, particularly for those areas and islands cut off from the main areas of economic activity.

users. Moreover these reforms should ensure greater competition both within and among the public ports.

Such a reform effort would cover a broad policy agenda, and would likely include a number of important measures such as the establishment of an independent regulatory authority, the decentralization and deregulation of port charges, allowing shippers to invest in and operate ports, deregulating ro-ro shipping and allowing private ports to compete directly with public ports in servicing third-party cargo.

Given the brevity of this paper we are unable to consider fully each of these important reform issues. Instead we focus on the last measure. That is, deregulation to allow ‘special’ purpose private ports, with appropriate facilities that would otherwise be generally under utilized, to accommodate third party cargo. This is a relatively simple measure that would inject much needed competition into the ports system.

### **Deregulation of special ports**

An important missing element in the Indonesian port sector is an effective regulatory framework that promotes competition and prevents the exploitation of market power. As noted early, every commercial public port in Indonesian is controlled by one of the four state owned enterprises, IPCs 1 to 4. In addition to being the major players in the port system, the present maritime law (Law 21/1992) also bestows considerable regulatory authority upon these public enterprises. The IPCs are in effect both player and regulator, and this has led to an abuse of market power

This is no more apparent than in the case of Indonesia’s special ports, which are regulated in such a way as to prevent direct competition with IPC ports. The decentralisation process however, has injected a new variable into this equation in the form of local governments pushing to take over the regulatory authority of regional ports. Although local governments are clearly acting in self-interest, this has the potential to deliver much needed competition into the port system providing real benefits for port uses.

As noted earlier, Indonesia has around 1400 ‘special ports’ that serve private sector needs in industry, mining, fishing etc. Some of these ports have facilities that are appropriate for only one or a group of commodities (e.g. chemicals) and have limited capacity for the accommodation of third party cargo. Others, however, have facilities appropriate for a broad range of commodities, including in some cases, containerised cargo. In any case, special ports are forbidden, by way of Law 21/1992, to provide services for third party cargo, except in the following circumstances:

- IPC ports in the region do not have sufficient capacity to provide adequate port services or have been damaged by a natural disaster or other event, or
- There are no IPC ports in the region that can provide the required services

Whenever it is the case that a special port is authorised to accommodate third party cargo, it must then work closely with, and report to the particular IPC that has the authority to regulate that part of the coastline (note the areas of control as described in Introduction section). As part of this cooperation, the IPC sets fees and charges. To ensure no price competition, port charges at the IPC port applies at the special port. Moreover, 100% of the port charges are collected by the IPC,

whilst the revenues from the other charges (such as dockage and wharfage fees) are split with the special port.

## **Decentralization of the Ports Sector**

Since decentralization commenced formally at the beginning of 2001, there has been a very public, and to this day unresolved dispute between the central government represented by the Department of Communications and a group of local governments led by the District of Cilegon, in the province of Banten.

At the core of this dispute is the authority to regulate special ports<sup>18</sup>. The matter is complicated by the conflicting nature of the maritime and decentralization laws. The maritime laws empower the IPCs as the key port operators and regulators in the regions. The decentralization laws and regulations, on the other hand, devolve most authority on ports to the regions.

This is a common problem in Indonesia. Many laws governing particular sectors have yet to be amended to accommodate regional autonomy. This can be explained in part by the swift manner in which the decentralization law was drafted and implemented, leaving technical departments little time to consider and suggest appropriate legislative adjustments. Reluctance on the part of central government officials, and their colleagues in central government owned enterprises to cede technical authority to the regions may also play a role.

### **Box 2**

#### **Decentralization Laws and Regulations**

The Decentralization law has provisions defining what governance authorities are given to regional authorities and what are retained by the central government. Articles 7 (1) and 7 (2), for example, outlines which areas are to remain as matters of ‘national concern’ and therefore not to be devolved to the regions. These include international politics, defense, justice, monetary and fiscal policy, religion, national planning, national macroeconomic development, national administration, human resource development, exploitation of natural resources, strategic high technology, conservation and national standards. Article 11, of the same law clearly states that transportation authority is to be devolved to the regions.

The supporting regulation (PP 25/2000) provides in greater detail a delineation of central and local government authority. For each sector, it lists what matters must remain as a matter of national interest. All residual authority is ceded to the regions. In the area of sea transport central government authority is limited to the provision of guidelines for the location of major seaports, establishment of shipping channels, standards for the transport of hazardous materials, the navigation, guiding and tugging of ships, surveillance and rescue operations, standards for the management of piers, provision of facilities beyond the 12 mile limit, establishing standards on workplace environments within seaports, the licensing of dredging beyond the 12 mile limit, and standards for ocean worthiness.

The major complaint by local governments such as Cilegon is that they, and not the IPCs should have the authority to regulate regional ports, in particular the ports owned and operated by the private sector. They note that the IPCs impose various levies and charges upon users of non-IPC ports, but there is often little, if any, link between payment and services rendered.

---

<sup>18</sup> Although local governments would clearly like to expand their authority to regulate all commercial ports, including public IPC ports, within district borders.

## **The Case of Cilegon**

Cilegon is a district in the newly established province of Banten, located in the western part of Java, approximately two hours by car to the west of Jakarta. The district covers much of the Java coastline of the Sunda Strait, a major shipping lane. It is also an important center for key manufacturing activities such as steel, chemicals, paper etc.

Despite the district's strategic location and its concentration of industries, the district does not have a major public port. The largest IPC port is the port of Ciwandan. However the port is poorly equipped, and is in need of major upgrading if it is to adequately provide port services to local industries. For these and other reasons, the district has within its borders 18 special ports developed for private industrial use (two of which are described below). The ports sector is therefore very important to the district government of Cilegon. Unsurprisingly, the first by-law produced by this district government concerned the administration and regulation of regional ports (*Perda* 1/2001)

### **Port of Cigading (Krakatau Steel)**

Much of the dispute between the central government and the administration in Cilegon centres on the port of Cigading, a special port privately operated by PT Krakatau Bandar Samudera (KBS a subsidiary of the state-owned Krakatau Steel Group). The port is situated near the Sunda Strait and is one the deepest port in Indonesia. With a low water surface of 20 meters, the port can accommodate Cape-size vessels up to 150,000 DWT (larger than that of nearby Tanjung Priok, Jakarta).

Cigading is a large port with a capacity well beyond that required to service the Krakatau Steel plant. Even after being licensed to handle some third party cargo by IPC II, Cigading was operating well under capacity. This was a matter of some frustration for Cigading port officials, as they could offer superior services (as measured by costs and time at port) than that of nearby IPC II ports<sup>19</sup>, but were only able to accommodate ships whenever explicitly approved by IPC II. Moreover, despite being more competitive, fees and charges applied were determined by IPC II.

As noted above, the local government of Cilegon has issued and implemented a by-law (1/2001) that seeks to take over the regulatory functions of the IPC, and ultimately to promote competition within district ports through deregulation. Under a special arrangement, there is now no restriction upon the Cigading special port providing services to third party cargo. Surcharges for wharfage and dockage previously assessed at 50% by IPC-II have been lowered to 20% this local by-law. More importantly shippers now have a choice of either Cigading or one of the nearby IPC ports, as opposed to only having access to Cigading whenever the IPC ports are full. This is an important point, as access to the port means much less turnaround time, which translates into significant savings for shipping.

---

<sup>19</sup> Cigading officials maintain that their cargo handling costs are 15-20% lower than Tanjung Priok, Jakarta. Moreover the port requires less than half the time to unload a 60,000-ton vessel in the same port.

Cilegon is an important test case for the central government. Many other local governments (with private ports within their jurisdictions similarly equipped to accommodate third party cargo) have been in contact with the city authorities in Cilegon and are now considering similar legislation<sup>20</sup>. The central government initially responded by challenging the legality of the Cilegon by-law. The Ministry of Home Affairs, which has the authority to rescind local regulations, has written to the Mayor of Cilegon requesting that the by-law is withdrawn. To date, these and other requests have been refused. The Cilegon government has argued a convincing case for its right to regulate special ports, and has fully exploited the relevant clauses in both the decentralization and competition laws.

Interestingly, Cilegon's by-law on ports has yet to be included as one of the 80 local regulations deemed by the Ministry as 'problematic' and therefore to be rescinded. Almost all of these regulations are nuisance taxes and charges, with no real benefit for the community. The Cilegon ports by-law on the other hand is clearly in the public interest, as it reduces port costs and introduces an element of competition into an otherwise monopolistic sector.

Aware of the general need to decentralize authority, and more specifically to respond to local government demands for greater say in how ports within their jurisdictions are managed, the Ministry of Communications recently announced in early September that 471 ports will be handed over to the regions (150 to Provincial governments and 321 to Municipal governments). However, to the disappointment of local governments, almost all of these ports were small and unprofitable. Few, if any, are frequented by commercial shipping. In what has been termed the 'Balikpapan Declaration', local governments, after meeting to discuss the plan, rejected it arguing that ownership and management of these ports would be an unwelcome economic burden. More cynically it was seen as an attempt by the IPCs to offload their loss making assets to local government. Clearly, there would have been a different response if some of the more commercially viable ports were to be devolved to the regions.

## **Conclusion**

This paper has provided a brief overview of the many problems confronting the Indonesian ports sector, such as congestion, poor management, inadequate facilities as well as regulatory and institutional constraints. With rapid growth in demand for port services expected in the short to medium term, perhaps a trebling of container traffic over the next 10 years, there is increasing urgency to find effective and sustainable remedies for these problems.

Port modernization and reform requires a number of measures covering a broad policy spectrum. Two such measures were discussed in this paper.

The first involves facilitating greater private sector investment in ports. Given limited public resources, there is now broad awareness that any major upgrading effort would need to be funded privately. The challenge in the short-medium term is to find appropriate models of public-private

---

<sup>20</sup> According to Cilegon government officers, this includes local governments from Serang, Gresik, Lampung, Cilacap and South Sulawesi.

partnership that can effectively marry the various stakeholder interests, in particular those of private investors and end-users.

The second measure discussed is to allow special purpose private ports to accommodate third party cargo – a measure that would inject much needed competition into an otherwise highly regulated and monopolistic sector. Under decentralization this entails important regulatory authority being devolved from the centre to the regions.

Implicit in each measure, be it privatization or decentralization, is a general dilution of the role of the state-owned Indonesian Port Corporations.